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The Director of Central Intelligence

Washington, D.C. 20505

National Intelligence Council

NIC 02112-87
15 May 1987

MEMORANDUM FOR: Acting Director of Central Intelligence

FROM: Maj Gen Frank B. Horton III, USAF
Chairman

SUBJECT: DIA Request for Dollar Costing Estimate

1. Action: your approval and signature on the attached letter to General Perroots agreeing to an NFIB-approved IIM on the methodology for dollar costing of military expenditures. The letter does not, however, propose to cover results in the IIM, or alternatively to cover results as part of an extended set of joint CIA-DIA produced, Military Board approved papers. The latter procedure, we believe, should be reserved as it is today for those exceptional products aimed at audiences that clearly require a coordinated administration view such as our annual joint JEC testimony. Results, for the most part, would continue to be published by individual agencies in papers that would be based on the proposed IIM.

2. Background. The Perroots request for Community papers asked for (a) Community approval on a paper on the methodology of dollar costing including the strengths, weaknesses, and caveats of the techniques and (b) Community agreed results of a comparison of NATO-Warsaw Pact defense costs using these techniques. General Durkin told me that Perroots was primarily after a Community paper on methodology rather than one on results. Hence, by agreeing to an IIM on dollar costing methodology only, I believe we are responding adequately to the substance of the request.

3. As to the possibility of expanding joint CIA-DIA production and Military Costing Review Board approval of results-oriented dollar costing papers, Deane Hoffmann and I believe in our consultations with SOVA that we should continue to allow individual agency production of most results-oriented papers. We could still serve the purpose of enhancing their consistency and assuring their caveating by using the forthcoming IIM as a mandatory basis for doing the work and putting it in proper context. To go further and insist on joint production and approval of such papers in other than special cases agreed between DIA and CIA like the JEC testimony, we believe, would do a disservice to competitive analysis while hampering the production process.

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4. Thus, unless you feel strongly about expanded joint production and approval of such papers, propose that we proceed as indicated and that you sign out the attached. If you wish to discuss the issue of joint analyses further, however, I recommend you, I, Deane Hoffmann, and [redacted] DI/SOVA, get together to air further the possible benefits and potential pitfalls. 25X1

Very respectfully,

MGen Frank B. Horton III

Attachment:
Memo to LtGEN Perroots, D/DIA

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SUBJECT: DIA Request for Dollar Costing Estimate

NIO/Econ/DHOFFMANN:rr [redacted] 15 May 1987 NIC 02112-87 25X1

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The Deputy Director of Central Intelligence

Washington, D.C. 20505

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87-1924

18 MAY 1987

MEMORANDUM FOR: Lieutenant General Leonard H. Perroots, USAF
Director, Defense Intelligence Agency

SUBJECT: Request for National Intelligence Estimate on Dollar Costing of Warsaw Pact Military Spending

1. I agree with you that dollar cost comparisons of Soviet-US and NATO-Warsaw Pact defense costs, while useful, have limitations and are frequently misunderstood by policymakers. Hence, a paper that clearly lays out the approved methodology, its alternatives, their strengths and limitations, and the caveats that should accompany their use, would be a useful piece as background for our readers. I would include in this paper our recent addition to the dollar costing methodology for non-US NATO countries to account for currency fluctuations that was recently briefed to our joint CIA/DIA Military Costing Review Board and to you and your staff.

2. I believe such an overview paper should be drafted jointly by CIA and DIA, sent to the joint Military Costing Review Board for approval of the portrayal of the methodology, its alternatives, and appropriate caveats, then more widely coordinated throughout the Intelligence Community and reviewed by the NFIB before being published as an Interagency Intelligence Memorandum. I would ask the NIO for Economics to oversee the process. It is important to note that the joint Board-approved dollar cost estimating techniques that would be highlighted in this paper were thoroughly reviewed in 1983 by a group of outside experts, the DCI's Military-Economic Advisory Panel (MEAP). Only one relatively minor extension has been made in the methodology since then, the one applying to non-US NATO countries noted above, and these experts have been asked to review this change.

3. Your letter also suggests that the proposed paper include results of the application of the methodology in the context of a NATO-Warsaw Pact spending comparison. I would prefer to leave to other papers the detailed application of the methodology, on an as needed basis, although the paper in question would no doubt have to illustrate the points it makes. I believe such largely technical results-oriented papers should continue to be produced primarily by the individual agencies, basing their work on the

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methodologies and caveating their results using the language that will appear in the proposed IIM. This strikes the right balance between Community consistency and competitive analysis, it seems to me. I would reserve for joint production and Costing Board approval those especially significant papers that we agree should be joint given their audiences, currently the annual JEC testimony on the Soviet economy and the biennial paper for NATO presentation on NATO-Warsaw Pact Defense costs.

/s/ Robert M. Gates

Robert M. Gates
Acting Director

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DEFENSE INTELLIGENCE AGENCY

WASHINGTON, D.C. 20340- 6134

17 APR 1987

U-0675/DE-1

MEMORANDUM FOR THE DIRECTOR OF CENTRAL INTELLIGENCE

SUBJECT: Request for National Intelligence Estimate on Dollar Costing of Warsaw Pact Military Spending

1. The current methodology used for costing Soviet and non-Soviet Warsaw Pact (NSWP) defense efforts in dollar terms has been in use for a number of years. It has required considerable effort and resources, mostly on the part of CIA, but to some extent on the part of other agencies as well. Given this investment, we believe that now is an appropriate time to take a fresh look at this direct costing methodology, particularly as a new generation of weapons begins production and requires new costing efforts.

2. There has been increasing use of dollar cost comparisons of Soviet-U.S. and NATO-Warsaw Pact defense costs, but often with insufficient understanding on the part of policymakers as to how and why we do such costing and its limitations. A definitive document on dollar costing would serve to clarify a number of issues.

a. It would provide community agreed results of such comparisons as NATO and Warsaw Pact costs and Soviet and U.S. defense costs.

b. It would provide the strengths and weaknesses of the methodology, the definitions (i.e., inclusions and omissions) used in making the estimates, the limitations of the data itself, the confidence levels associated with the various parts of the methodology making up the estimate, and the caveats on the use of the estimates.

c. It would address the detail of the methodology itself, to include such items as the costs of the equipment, the last time such items were costed, and the various ways in which different items are actually costed.

d. It could also provide a review of the non-U.S. NATO costs and their applicability to these comparisons.

3. The review of the methodology would serve as a basis for an assessment of our ability to cost the next generation of weapons systems, and to identify the extent of the gaps in our knowledge of weapon systems.

4. Through the process of developing our own budget proposals, we expect that policymakers will rely even more on dollar cost comparisons. The usefulness of such comparisons would be greatly

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enhanced if we could provide a better understanding of the methodology involved and the limitations of the numbers contained in the estimates.

5. DIA strongly recommends that an estimate on Soviet and NSWP dollar costing be undertaken, as well as a review of non-U.S. NATO costs. DIA is prepared to provide full support to this effort. In view of the importance of the issue, we hope that work on this estimate could begin soon.

Leonard H. Perroots

LEONARD H. PERROOTS
Lieutenant General, USAF
Director

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